Supreme Court, U.S.
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ALEXANDER L. STEVAS,
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No. 82-1579

IN THE

Supreme Court of the United States

October Term, 1982

HAYFIELD NORTHERN RAILROAD COMPANY, INC., *Appellant,*

and

STATE OF MINNESOTA, *Appellant/Intervenor,*

vs.

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY, *Appellee.*

On Appeal From the United States Court of Appeals for the Eighth Circuit

APPENDIX TO MOTION TO AFFIRM

Of Counsel:
THOMAS E. GLENNON
LINDQUIST & VENNUM
4200 IDS Center
80 South Eighth Street
Minneapolis, Minnesota 55402
(612) 371-3211
JAMES P. DALEY
ANNE E. KEATING
CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY
One North Western Center
165 North Canal Street
Chicago, Illinois 60606
(312) 559-6072

EDWARD M. GLENNON
4200 IDS Center
80 South Eighth Street
Minneapolis, MN 55402
(612) 371-3211
STUART F. GASSNER
One North Western Center
165 North Canal Street
Chicago, Illinois 60606
(312) 559-6072
Attorneys for Appellee Chicago and North Western Transportation Company

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APPENDIX

APPENDIX A

46 Fed. Reg. 36,763 (No. 135)
Wednesday, July 15, 1981

[No. AB-1 (Sub-No. 113)F]

Chicago and North Western Transportation Company—Abandonment Between Oelwein, IA and Randolph, MN; Findings

July 10, 1981.

Notice is hereby given pursuant to 49 U.S.C. 10903 that by a decision decided July 10, 1981, a finding, which is administratively final, was made by the Administrative Law Judge stating that, the public convenience and necessity permit the abandonment by The Chicago and North Western Transportation Company of a line of railroad extending from railroad milepost 354.3 near Oelwein, IA to milepost 457.2 near Dodge Center, MN, from milepost 459.0 north of Dodge Center to milepost 496.9 near Randolph, MN, and from milepost 1.2 at Hayfield, MN to milepost 5.2 at Waltham, MN, a total of 144.8 miles traversing Fayette, Bremer, Chickasaw, Howard and Mitchell Counties in Iowa, and Mower, Dodge, Goodhue, Rice and Dakota Counties in Minnesota. Abandonment is subject to the conditions for the protection of employees discussed in *Oregon Shortline Railroad Co.—Abandonment—Goshen*, 360 I.C.C. 91 (1979). A certificate of abandonment will be issued to The Chicago and North Western Transportation Company based on the above-described finding, 30 days after publication of this notice, unless within 15 days from the date of publication, the Commission further finds:

(1) a financially responsible person (including a government entity) has offered financial assistance (in the form of a rail service continuation payment) to enable the rail service involved to be continued. The offer must be filed with the Commission and served concurrently on the applicant, with copies to Mrs. Ellen Hanson, Room 5417, Interstate Commerce Commission, Washington, DC 20423, no later than 10 days from publication of this Notice; and

(2) It is likely that such proffered assistance would:

(a) Cover the difference between the revenues which are attributable to such line of railroad and the avoidable cost of providing rail freight service on such line, together with a reasonable return on the value of such line, or

(b) Cover the acquisition cost of all of any portion of such line of railroad.

If the Commission so finds, the issuance of a certificate of abandonment will be postponed. An offer may request the Commission to set conditions and amount of compensation within 30 days after an offer is made. If no agreement is reached within 30 days of any offer, and no request is made of the Commission to set conditions or amount of compensation, a certificate of abandonment will be issued no later than 50 days after notice is published. Upon notification to the Commission of the execution of an assistance or acquisition and operating agreement, the Commission shall postpone the issuance of such a certificate for such period of time as such an agreement (including any extensions or modifications) is in effect. Information and procedures regarding the financial assistance for continued rail service or the acquisition of the involved rail line are contained in 49 C.F.R. §1121 as revised by Ex Parte No.

274 (Sub-No. 6), *Abandonment of Railroad Lines and Discontinuance of Service*, 45 FR 75144 (November 25, 1980). All interested persons are advised to follow the instructions contained therein as well as the instructions contained in the above-referenced decision.

Agatha L. Mergenovich,
Secretary.

APPENDIX B

BEFORE THE
INTERSTATE COMMERCE COMMISSION

CHICAGO AND NORTH WESTERN TRANSPORTATION COMPANY—ABANDONMENT BETWEEN OELWEIN, IOWA AND RANDOLPH, MINNESOTA

Docket No. AB-1
(Sub-No. 113F)

OFFER OF FINANCIAL ASSISTANCE RELATING TO PORTIONS OF LINE BETWEEN MILEPOSTS 442 AND 457.2 AND BETWEEN MILEPOSTS 1.2 AND 5.2

BROWNSDALE COOPERATIVE ASSOCIATION
CENTURY PLASTICS, INC.
FARMERS COOPERATIVE OIL ASSOCIATION
MIDLAND COOPERATIVES, INC.
MOWER COUNTY SERVICE COMPANY
POWER SPAN, INC.
REESE FARM CENTER, INC.
Offerors

FREDERICK A. MUTH, JR.
DAVID C. HERTEL
Whyte & Hirschboeck, S.C.
2100 Marine Plaza
Milwaukee, Wisconsin 53202

THOMAS F. McFARLAND, JR.
20 North Wacker Drive
Chicago, Illinois 60606
(312) 236-0204
Attorneys for Offerors

BELNAP, McCARTHY, SPENCER,
SWEENEY & HARKAWAY
Of Counsel
Due Date: July 24, 1981

STATEMENT OF THE CASE

On January 30, 1981, Chicago and North Western Transportation Company (C&NW) filed an application for authority to abandon its line of railroad between Oelwein, Iowa and Randolph, Minnesota.

An investigation was instituted into the proposed abandonment. Hearings were held at Oelwein, Iowa on May 5-8, 1981.

Among the parties protesting the proposed abandonment in whole or in part was a group of shippers and receivers located on those portions of C&NW's line between Dodge Center and Sargeant, Minnesota (Mileposts 442-457.2), and between Hayfield and Waltham, Minnesota (Mileposts 1.2-5.2). That group includes the parties making this offer of financial assistance.

That group of Minnesota shippers opposed the proposed abandonment insofar as it included the 19.2-mile segment of line on which they are located. Those shippers introduced evidence that operation of that segment was

profitable to C&NW in the base year, and would be even more profitable in the immediate future. C&NW did not attempt to rebut that evidence.

In an initial decision served July 15, 1981, Administrative Law Judge (ALJ) Paul J. Clerman found that the proposed abandonment should be authorized in full. The ALJ summarized the evidence of the Minnesota shippers at page 13 and Appendix E of the initial decision, but he concluded that their proposal was not drawn with sufficient detail to permit comprehensive analysis as to profitability (page 23).

The findings of the initial decision were published in the *Federal Register* of July 15, 1981. Pursuant to interim rules adopted in Ex Parte No. 274 (Sub-No. 6), *Abandonment of Railroad Lines and Discontinuance of Service*, 45 FR 78144 (Nov. 25, 1980), offers of financial assistance for continued operation of the line, if any, must be filed on or before Friday, July 24, 1981.

Administrative appeals of the initial decision, if any, must be filed on or before August 4, 1981.

FOREWORD

The Minnesota shippers filing this offer of financial assistance intend to subsidize continued operation of the 19.2-mile segment of line only in the event that the Commission's final decision is that abandonment of that segment is permitted by public convenience and necessity. Depending upon the Commission's decision in that respect, judicial review of that decision may also be sought. Consequently, those shippers intend to pursue their administrative remedy with respect to the merits of the initial decision relating to that segment and, if necessary and appropriate,

the shippers will also pursue their judicial remedy in that respect.

However, the Commission's current practice of publishing the findings of its initial decisions authorizing abandonments in the *Federal Register* as notice of the opportunity to offer financial assistance as to the involved lines, as if such initial decision findings were final Commission findings, requires potential offerors to make "protective" offers of financial assistance, such as this offer, before pursuing their legal remedies on the merits of the abandonments. That is so because otherwise the 10-day deadline for offering financial assistance arguably would have expired by the time review of the merits of the abandonment had been completed. In our view, that practice clearly violates 49 USC §10905(c), read together with 49 USC §10904(c)(3).

In any event, this offer of financial assistance is filed pursuant to 49 CFR §1121.38 (interim), as interpreted in *Illinois Central Gulf Railroad Company—Abandonment—between Herscher and Barnes in Kankakee, Ford, Livingston, and McLean Counties, IL*, Docket No. AB-43 (Sub-No. 43), decided April 28, 1981 (not printed).

The offerors seek a finding that they are financially responsible persons who have made an adequate offer of financial assistance for continued operation of the 19.2-mile segment of line in Minnesota.

OFFER OF FINANCIAL ASSISTANCE

Pursuant to 49CFR §1121.38(c)(2) (interim), Brownsdale Cooperative Association; Century Plastics, Inc.; Farmers Cooperative Oil Association; Midland Cooperatives, Inc.; Mower County Service Company; Power Span,

Inc.; and Reese Farm Center, Inc. hereby offer financial assistance for continuation of rail service on the 19.2-mile segment of C&NW's line between Dodge Center and Sargeant, Minnesota (Mileposts 442-457.2), and between Hayfield and Waltham, Minnesota (Mileposts 1.2-5.2), and make the following showing in support of such offer:

49 CFR §1121.38(c)(2)(i)

Offer and Proposed Subsidy Payment

The offer of financial assistance is to subsidize continued operation over the 19.2-mile segment during the subsidy period. The offer contemplates that such subsidy would consist of payment for (1) the excess of avoidable costs of operating the line segment over the revenues attributable thereto, if any, based upon actual operations conducted during the subsidy period; (2) administrative costs based upon one percent of the actual revenues attributable to the line segment during the subsidy period; and (3) a reasonable return on the value of the line segment—all as determined pursuant to the methodology for subsidy calculations contained in 49 CFR Part 1121, Subpart D. See decision of April 28, 1981 in Docket No. AB-43 (Sub-No. 43), *supra*, pp. 5-6.

The following proposed subsidy payment is submitted for illustrative purposes only. It shows the subsidy which would have been required if subsidized operations over the line segment had been conducted during the base year ended July 31, 1980. See decision of April 28, 1981 in Docket No. AB-43 (Sub-No. 43), *supra*, page 6. The source of the data for the calculation of the payment is the unrebutted evidence of Witness George C. Shaffer in the abandonment proceeding, Exhibit 18, modified, as neces-

sary, by the findings of ALJ Clerman in the initial decision. The foremat for illustration of the estimated subsidy is that contained in the appendix to the decision of April 28, 1981 in Docket No. AB-43 (Sub-No. 43), *supra*. The basis for the calculations is briefly explained following the illustration of the payment:

Proposed Subsidy Payment
Mileposts 442-457.2 and 1.2-5.2

Base Year Operations—Illustrative Purposes Only

1.	Revenues			$162,443
2.	Avoidable Costs			73,769
	a. Off-branch			
	b. On-branch			
	1. Maint.-way	$	5,304	
	2. Maint.-equip.		1,514	
	3. Transp.		10,990	
	4. Deadheading		150	
	5. Car Cost		3,953	
	6. Return-loco.		1,892	23,802
3.	Total Avoidable Cost			$ 97,571
4.	Return on Value			
	a. Working Capital	$	978	
	b. Net Liquidation Value		1,739,848	
	c. Total Valuation		1,740,826	
	d. Rate of Return		9.3%	
	e. Return on Value			161,897
5.	Administrative Costs (1% of revenues)			1,624
6.	Estimated Subsidy Payment (Line 1 minus Lines 3, 4e and 5)			$ 98,649

The revenues shown on line 1 of the above calculation are the actual C&NW revenues derived from 217 carloads of traffic originated or terminated on the 19.2-mile segment in the base year (Ex. 18, p. 14; initial decision, p. 13).

Off-branch costs shown on line 2a of the calculation are Rail Form A off-branch costs for those 217 carloads as applied by C&NW, except that the costs for switching at the Dodge Center junction are C&NW's Rail Form A costs for inter/intra train switching, rather than modified terminal costs used by C&NW (Ex. 18, pp. 11-12; initial decision, p. 13).

On-branch costs shown on line 2b of the calculation are based on actual costs developed by C&NW, prorated and allocated to those 217 carloads of traffic on the basis of gross ton-miles, car-miles and car-days (Ex. 18, p. 13; initial decision, p. 13).

Total avoidable costs shown on line 3 are the sum of off-branch costs and on-branch costs shown on lines 2a and 2b, respectively.

Return on value shown on line 4e was derived by applying a rate of return of 9.3 percent (line 4d) to the sum (line 4c) of working capital and the net liquidation value of the line segment (lines 4a and 4b, respectively). The rate of return is that used in the decision of April 28, 1981 in Docket No. AB-43 (Sub-No. 43), *supra*, p. 10. Working capital on line 4a was computed at 15 days of on-branch cash avoidable costs in the base year. *Id*, p. 7. In that respect, Witness Shaffer incorrectly estimated working capital on the basis of a mileage prorate to the 19.2-mile segment of working capital assigned to the entire line by C&NW (Ex. 18, p. 15). Net liquidation value was determined by adding (1) the land value in the 19.2-mile seg-

ment on the basis of a mileage prorate to that segment of total land value for the entire line, and (2) the net salvage value of the actual track materials in the segment as valued by C&NW; however, that net salvage value was adjusted downward on the basis of the reduced values of usable rail found in the initial decision (Ex. 18, p. 15, Ex. GCS-4; initial decision, pp. 10-11, 19).[1]

Administrative costs on line 5 represent one percent of the actual revenues on segment traffic in the base year. See decision of April 28, 1981 in Docket No. AB-43 (Sub-No. 43), *supra*, p. 10.

The estimated subsidy payment on line 6 represents the amount by which the return on value of the line plus administrative costs exceed the operating profit achieved in the base year. Once again, it is emphasized that the above calculation is an illustration of the subsidy methodology, not an offer to pay a specific dollar amount of subsidy. See decision of April 28, 1981 in Docket No. AB-43 (Sub-No. 43), *supra*, p. 11.

49 CFR §1121.38(c)(2)(ii)

Authorization to Execute and Fulfill Agreement to Subsidize

Each of the seven companies filing this offer of financial assistance has corporate authority to execute and to fulfill

[1]Witness Shaffer valued all usable rail at $312.90 per ton, on the basis of C&NW's valuation (Ex. 18, Ex. GCS-4, p. 2). The initial decision found that usable 115-pound rail should be valued at $275 per ton; usable 112-pound rail should be valued at $270 per ton; usable 100-pound rail should be valued at $235 per ton; and usable 90-pound rail should be valued at $225 per ton (initial decision, pp. 10, 19). The resulting recalculation reduces the gross value of rail in the 19.2-mile segment by $207,548, and correspondingly reduces the net liquidation value of that segment from $1,947,396, as testified by Witness Shaffer, to $1,739,848.

an agreement to subsidize continued operation of the 19.2-mile segment of rail line. Appendix 1 to this offer consists of written resolutions and/or authorizations to that effect.

49 CFR §1121.38(c)(2)(iii)

Information Relating to Sufficiency of Financial Resources for Subsidy

Appendices 2 and 3 to this offer consist of recent balance sheets and profit and loss statements, respectively, for six of the seven companies joining in this offer of financial assistance. (Similar documents for the seventh company, Midland Cooperatives, Inc., were not available in the short period of time within which this offer must be made.) It is submitted that those financial statements demonstrate the sufficiency of the financial resources of those companies to provide subsidy payments of the magnitude shown in the illustration of estimated subsidy payment for continued operation of the 19.2-mile segment. In addition, the following information is submitted in support of the sufficiency of the financial resources of those companies.

Brownsdale Cooperative Association is a farm supply cooperative with principal place of business located at Brownsdale, Minnesota. It has approximately 800 farmer member-stockholders. At Brownsdale, the Association owns offices, a grain elevator, a fertilizer blending plant and a feed facility. It also owns a fertilizer blending plant located at Waltham, Minnesota. The gross sales of Brownsdale Cooperative Association were approximately $9.2 million in 1980.

Century Plastics, Inc. is engaged in the manufacture and

sale of corrugated drainage tubing for agricultural use at Hayfield, Minnesota. The company owns a 5,400 square-foot warehouse and a 4,900 square-foot production facility. Those facilities have been located at Hayfield since 1972. The gross sales of Century Plastics, Inc. were approximately $2 million in 1980.

Farmers Cooperative Oil Association is a farm supply cooperative organized in 1924. It has approximately 800 farmer member-stockholders. Its principal place of business is located at Hayfield, Minnesota. There it owns a service station, office, warehouse, fertilizer plant and bulk petroleum facility. The gross sales of Farmers Cooperative Oil Association were approximately $3.2 million in 1980.

Midland Cooperatives, Inc. is an association of farm cooperatives with its principal place of business located at Minneapolis, Minnesota. Midland supplies fertilizer, seed chemicals, petroleum, LP gas, hardware and feed to farm cooperatives in the Midwest. It also manufactures liquid fertilizer. Midland owns a liquid fertilizer manufacturing plant at Hayfield, Minnesota.

Mower County Service Company is a farmer-owned cooperative engaged in the retail sale of fertilizer, chemicals, petroleum products, feed and hardware to farmers in Mower County, Minnesota. The company has been in existence for approximately 10 years, and has between 800 and 1,000 farmer member-shareholders. At Sargeant, Minnesota, the company owns a general office, hardware store, warehouses for chemicals, feed and petroleum, service stations, a petroleum plant and fertilizer plants. At Waltham, Minnesota, the company owns a petroleum product service station. At Adams, Minnesota, the company owns a service station, bulk petroleum plant, feed warehouses and a fertilizer plant and

warehouse. The gross sales of Mower County Service Company were approximately $5 million in 1980.

Power Span, Inc. is engaged in the business of manufacturing pre-stressed concrete poles used for electrical power transmission. Its manufacturing facility is located at Hayfield, Minnesota. Power Span's plant in Hayfield was purchased in late 1979 for in excess of $4 million. Power Span employs approximately 75 persons at Hayfield.

Reese Farm Center, Inc. is engaged in the retail sale of agricultural supplies. It also leases farm land and plants and harvests grain. Reese farms 1,830 acres of leased land in the area of Hayfield, Minnesota. At Hayfield, Reese owns an office building, fertilizer mixing and storage warehouse, machine shed and feed warehouse, a flat grain storage building with capacity of 125,000 bushels, a shop, a chemical warehouse, two bulk agricultural chemical tanks and nine liquid fertilizer tanks. Reese also owns a seed storage facility, a grain dryer and grain storage bins with capacity of 73,000 bushels at that location. The gross sales of Reese Farm Center, Inc. were $2,054,000 in 1980.

Collectively, the seven companies offering financial assistance in this proceeding are properly characterized as financially responsible. As demonstrated above, their collective ownership of assets is very extensive, and their 1980 gross sales number in the tens of millions of dollars. There is no question that they could adequately fund an estimated subsidy payment of the magnitude of that shown in the illustration above.

49 CFR §1121.38(c)(2)(iv)

Adequacy of Offer to Cover Avoidable Loss Plus Reasonable Return on Value

As demonstrated in detail in the response to 49 CFR §1121.38(c)(2)(i), this offer is specifically designed to cover the avoidable loss incurred in operating the 19.2-mile segment of line in the subsidy period, if any, plus administrative costs and a reasonable return on the value of that segment, all as determined pursuant to the methodology prescribed in 49 CFR §1121, Subpart D. The illustration of estimated subsidy payment if operation of that segment had been subsidized in the base year provides an "order of magnitude" of the extent of this offer. It is recognized, however, that the actual subsidy during the subsidy period will depend upon the results of operations during that period. That concept is consistent with the decision of April 28, 1981, in Docket No. AB-43 (Sub-No. 43), *supra*.

49 CFR §1121.38(c)(2)(v)

Carrier's Estimated Subsidy

C&NW has not provided an estimate of the amount of subsidy which would be required to continue rail service on the 19.2-mile segment.

49 CFR §1121.38(c)(3)(i)

Current Balance Sheets

Appendix 2 to this offer contains the following balance sheets:

Brownsdale Cooperative Association — as of May 31, 1981

Century Plastics, Inc. — as of June 30, 1981

Farmers Cooperative Oil Association — as of June 30, 1981
Midland Cooperatives, Inc. — not available as of filing of offer
Mower County Service Company — as of July 31, 1980 (with explanatory letter of July 23, 1981)
Power Span, Inc. — as of March 31, 1981 (with explanatory letter of July 23, 1981)
Reese Farm Center, Inc. — as of May 31, 1981

49 CFR §1121.38(c)(3)(ii)
Profit and Loss Statements

Appendix 3 to this offer contains the following profit and loss statements:

Brownsdale Cooperative Association—years ended July 31, 1980, July 31, 1979 and July 31, 1978
Century Plastics, Inc. — years ended January 31, 1981, January 31, 1980 and January 31, 1979; February 1, 1981 through June 30, 1981
Farmers Cooperative Oil Association — six months ended June 30, 1981 and six months ended June 30, 1980
Midland Cooperatives, Inc. — not available at time offer filed
Mower County Service Company — years ended July 31, 1980 and July 31, 1979
Power Span, Inc. — year ended December 31, 1980
Reese Farm Center, Inc. — not available at time offer filed

49 CFR §1121.38(c)(3)(iii)
Additional Information

No additional information is submitted.

CONCLUSION — REQUESTED FINDING

WHEREFORE, offerors respectfully request that the Commission find that they are a financially responsible person(s) who has submitted an adequate offer of financial assistance with respect to the 19.2-mile line segment identified herein.

Respectfully submitted,

BROWNSDALE COOPERATIVE ASSOCIATION
CENTURY PLASTICS, INC.
FARMERS COOPERATIVE OIL ASSOCIATION
MIDLAND COOPERATIVES, INC.
MOWER COUNTY SERVICE COMPANY
POWER SPAN, INC.
REESE FARM CENTER, INC.
Offerors

FREDERICK A. MUTH, JR.
DAVID C. HERTEL
Whyte & Hirschboeck, S.C.
2100 Marine Plaza
Milwaukee, Wisconsin 53202
THOMAS F. McFARLAND, JR.
20 North Wacker Drive
Chicago, Illinois 60606
(312) 236-0204
Attorneys for Offerors
BELNAP, McCARTHY, SPENCER,
SWEENEY & HARKAWAY
Of Counsel

July 24, 1981

APPENDIX C

INTERSTATE COMMERCE COMMISSION DECISION

No. AB-1 (Sub-No. 113 F)
CHICAGO AND NORTH WESTERN
TRANSPORTATION COMPANY—ABANDONMENT
—BETWEEN OELWEIN, IA AND
RANDOLPH, MN.

IN THE MATTER OF AN OFFER
OF FINANCIAL ASSISTANCE
Decided: July 29, 1981

By initial decision served July 15, 1981, an Administrative Law Judge approved the abandonment of this 144.8 mile line. The findings were published in the *Federal Register* of July 15, 1981. An offer has been filed by a group of Minnesota shippers to subsidize continued operation of the 19.2 mile segment of the line between Dodge Center and Sargent, MN and between Hayfield and Waltham, MN, if the abandonment is ultimately approved.

The shippers include:

(1) Brownsdale Cooperative Association, a farm supply cooperative at Brownsdale, MN, which had 1980 gross sales of $9.2 million;

(2) Century Plastics, Inc., a manufacturer and seller of corrugated drainage tubing at Hayfield, MN, which had gross sales of $2 million in 1980;

(3) Farmers Cooperative Oil Corporation, a farm supply cooperative at Hayfield, MN, which had gross sales of $3.2 million in 1980;

(4) Midland Cooperative, Inc., an association of farm cooperatives at Minneapolis, MN (financial information was not filed for this company);

(5) Mower County Services Company, a farmer-owned cooperative at Mower County, MN, which had gross sales of $5 million in 1980;

(6) Power Span, Inc., a manufacturer of pre-stressed concrete poles at Hayfield, MN, which purchased its plant at Hayfield, MN in late 1979 for more than $4 million; and

(7) Reese Farm Center, Inc. at Hayfield, MN, a retail seller of agricultural supplies, which had 1980 gross sales of $2,054,000.

The shippers offer to pay for (1) the excess of avoidable costs of operating the line segment over the revenues attributable to it, based upon actual operations conducted during the subsidy period; (2) the administrative costs based upon one percent of the actual revenues attributable to the line segment during the subsidy period and (3) a reasonable return on the value of the line segment, all as determined by the methodology contained in 49 CFR 1121, Subpart D. Under their methodology, the shippers calculated that the subsidy would have amounted to $98,649 for the base year period ending July 31, 1980.

The shippers have offered a reasonable methodology for calculating the subsidy, in accordance with our guidance in AB-43 (Sub-No. 43), *Illinois Central Gulf R. Co.—Abandonment* 363 I.C.C. 866 (1981).

I find:

1. The shippers are financially responsible persons who have offered financial assistance to enable rail transporta-

tion to be continued over a part of the railroad line to be abandoned.

2. It is likely that the assistance would be equal to the difference between the revenues attributable to that part of the railroad line and the avoidable cost of providing rail freight transportation on the line, plus a reasonable return on the value of the line.

3. The issuance of the abandonment certificate should be postponed to allow the parties to enter into an agreement to permit continuation of rail service over the line.

4. This decision does not significantly affect the quality of the human environment or energy consumption.

It is ordered:

1. The issuance of a certificate authorizing abandonment is postponed. The offerors may request the Commission to set conditions and amount of compensation on or before August 21, 1981. If no agreement is reached, and no request is made on the Commission to set conditions or amount of compensation, a certificate of abandonment will be issued if the initial decision, authorizing abandonment is approved by the Commission. Upon notification to the Commission of the execution of an assistance or acquisition and operating agreement, the Commission shall postpone the issuance of the certificate for such period of time as the agreement (including any extensions or modification)

is in effect. See 49 U.S.C. §10905, *as amended* by §402 of the Staggers Rail Act of 1980, Pub. L. 96-448.

2. This decision is effective on the date it is served.

By the Commission, Gary J. Edles, Director, Office of Proceedings.

AGATHA L. MERGENOVICH
Secretary

(SEAL)

APPENDIX D

INTERSTATE COMMERCE COMMISSION DECISION

Docket No. AB-1 (Sub-No. 113F)
CHICAGO AND NORTH WESTERN
TRANSPORTATION COMPANY—ABANDONMENT
BETWEEN OELWIN, IOWA, AND
RANDOLPH, MN

REQUEST TO ESTABLISH
CONDITIONS AND COMPENSATION
Decided: October 16, 1981

By decision served July 15, 1981, Administrative Law Judge (ALJ) Paul J. Clerman, approved the application of the Chicago and North Western Transportation Company (CNW) to abandon 144.8 miles of rail line in Fayette, Bremer, Chickasaw, Howard, and Mitchell Counties, IA and Mower, Dodge, Goodhire, Rices, and Dakota Counties, MN. The findings were published in the *Federal Register* on July 15, 1981.

The Brownsdale Cooperative Association, Century Plastics, Inc., Farmers Co-operative Oil Association, Midland Cooperatives, Inc., Mower County Service Company, Power Span, Inc., and Reese Farm Center, Inc. (Shippers Group) filed an offer to subsidize continued operation of 19.2 mile line segment between Dodge Center, (milepost 457.2) and Sargeant, MN (milepost 442.0) and between Hayfield (milepost 1.2) and Waltham, MN, milepost 5.2).

On July 30, 1981, the Director of the Office of Proceedings determined that the Shippers Group was a financially

responsible person making an adequate offer of financial assistance and postponed the issuance of the abandonment certificate pending the negotiations between the Shippers Group and CNW. On August 21, 1981, the Shippers Group asked us to establish the conditions and compensation for financial assistance, pursuant to 49 U.S.C. 10905.

Procedural Matter

The Shippers Group criticizes our procedures and time frames for financial assistance proceedings. It argues that *Federal Register* publication of our findings granting abandonment should not occur until our decision has become administratively final—30 days after issuance of the initial decision. It believes that if an appeal is not filed or not considered, publication can occur 30 days after service of the initial decision. But, if an appeal is filed and entertained, it believes no publication can occur before we have disposed of such an appeal.

We disagree with this interpretation. Section 10905 requires that: (1) the service of the initial abandonment decision on the parties and publication be concurrent; (2) the offer of financial assistance be made within 10 days of publication; (3) our findings concerning the financial responsibility of the offeror and the adequacy of the offer be made within 15 days of publication; and (4) the carrier or the financially responsible party request us to set conditions and amount of compensation within 30 days after the offer is made. The filing of an appeal does not interrupt this sequence of events. A subsidy offer must be filed before there has been a determination of whether an appeal will be entertained. See *Abandonment of R. Lines & Discontinuance of Serv.*, 365 I.C.C. 249, 257 (1981).

Discussion and Conclusion

49 U.S.C. 10905(f)(1)(B) provides that "the Commission shall determine the amount and terms of subsidy based upon the avoidable cost of providing continued rail transportation plus a reasonable return on the value of the line." Avoidable costs during the subsidy year will depend upon, among other factors, traffic levels, maintenance requirements, and the rate of inflation in the subsidy year. As we indicated in *Illinois Central Gulf, -R. Co.*, 363 I.C.C. 866 (1981), *(Bloomer Line)*, our objective is to assure that a subsidy determination bears a direct relationship to actual costs and to assure that *all* risks of unprofitable operations will be on the subsidizer. To do this, we have prescribed a methodology to be used in the calculation which will properly compensate the railroad for operations. This methodology is found at 49 C.F.R. 1121, subpart D. Our decision here will only illustrate how the methodology should be applied in those areas which are disputed.

In their projections of future subsidization costs, the parties differ on the following items: (1) net liquidation value; (2) rate of return; (3) on-branch costs for maintenance of way and structures; (4) the casualty reserve account; and (5) administrative costs. These disputed items, as well as the Shippers Group's concerns about frequency of service, are discussed below.

Net Liquidation Value. The amount of the subsidy is based, in part, upon a reasonable return on the value of the line. This is calculated by applying a reasonable rate of return on an investment base comprised of three elements: working capital; income tax benefits; and net liquidation value. There appears to be no dispute on the working capital and since CNW does not pay taxes, there are no income tax benefits.

The Shippers Group maintains that the proper net liquidation value of the line segement (sic) is $1,527,320. This figure is based on a land value of $195,098 plus net salvage value of track materials of $1,332,222. CNW proposes a figure of $1,791,354 which is based on land value of $252,000 plus net salvage value of track materials of $1,539,354.

Land value—The Shippers Group states that the $195,098 value it placed on the land is based on $827 per acre and a total acreage of 235.91. CNW's land value of $252,000 is based on an average of $1,142 per acre on the 185.52 acres for the line between Dodge Center and Sargeant, and an average of $794 per acre on the 50.39 acres between Hayfield and Waltham. The offeror argues that CNW's figure is based upon the highest and best use *for rail purposes*. CNW disputes this claim.

It appears that CNW followed the methodology provided in the regulations. It supplied data based upon the testimony of an expert witness. Since CNW took into account factors which could affect valuation, such as questionable titles, and made adjustments for size, shape, location and time necessary to effectuate sales of the property, we will accept its estimate. In contrast, offeror neither provided expert testimony nor data on comparable sales in the area.

Salvageable track material—CNW asserts that the value of the entire 22.9 mile line to be purchased (19.2 miles of main line and 3.7 miles of "other track") is $1,539,354. The Shippers Group makes two adjustments to this figure.

First, the Shippers Group asserts that the value for the entire 22.9 miles is only $1,510,291. However, the $29,063 difference between these estimates is not explained. Since the burden of proof is on the offeror, we will accept CNW's statement that the entire line is worth $1,539,354.

Second, the Shippers Group argues that a substantial portion of the 3.7 miles of "other track" is either not owned by CNW or is not required for subsidy operations. It thus substracted (sic) the pro rated value of 2.7 miles from its original $1,510,291 estimate. CNW states, however, that of the 3.7 miles of "other track", 0.42 mile of private siding was not included and the remaining 3.37 miles is necessary because it includes 1.05 miles of industrial sidings at Hayfield and 2.23 miles of side track through Hayfield which are used for providing service to shippers at Hayfield and Waltham, who are among the offerors.

We accpet (sic) CNW's calculations because CNW has already excluded the private sidings from its calculations and has stated that the side track is necessary to service some of the offerors. In conclusion, we find the net salvage value to be $1,539,354.

Rate of Return

The rate of return to be applied to the investment base is the carrier's current cost of capital, after adjustment for the effects of current Federal and State income taxes.

CNW argues that we should apply a rate of return of 12.1 percent. This rate used by the judge in the initial decision,[1] reflects the fair rate of return for the nation's railroads developed in *Adequacy of Railroad Revenue (1980 Determination)*, 364 I.C.C. 311 (1980), *(Revenue Adequacy)*.

Shippers Group urges us to use a rate of return of 9.3 percent. This rate, which represents the nation's railroads' pre-tax cost of capital adjusted for inflation,[2] was used in *Bloomer Line*.

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[1]In *Chesapeake and Ohio Railway Company—Abandonment—South Haven and Hartford* (not printed) decided August 28, 1981, we held that subsidy determinations made in initial decisions are not binding in a subsidy proceeding.

[2]See, *Texas and Pacific Railway Company Abandonment*, 363 I.C.C. 666 (1980).

Our subsidy regulations require that the rate of return be based on the carrier's own cost of capital. Neither party has submitted any data which reflects CNW's cost of capital. Both, however, have inidicated (sic) a willingness to rely on the cost of capital figures used in the *Revenue Adequacy* proceedings. Their only dispute concerns adjustments for inflation and taxes. In the absence of actual evidence, we believe that the railroad industry's cost of capital, properly adjusted, is a reasonable approximation of the return available to CNW. However, the actual subsidy amount must be computed by using the carrier's own cost of capital.[3]

Two adjustments are generally necessary. First, this cost of capital figure must be expressed in pre-tax terms, in accordance with our regulations at 49 C.F.R. 1121.45(a). If we use the statutory tax rate, the pre-tax cost of capital (before inflation) is 19 percent. However, as we noted above, CNW does not pay taxes. Thus the pre-tax cost of capital, adjusted for CNW's actual taxes remains 12.1 percent.

We believe that this pre-tax cost of capital may overstate the rate of return required to compensate the carrier adequately. Without an adjustment it is possible that inflation may be double counted since (1) the pre-tax cost of capital which reflects the impacts of inflation and (2) the value of the rail operating property may appreciate in time solely due to inflation.

In order to prepare a reasonable rate of return, the annual increase to the value of rail property due solely to inflation

[3]An acceptable method for calculating a carrier's individual cost of capital is contained in the *Revenue Adequacy* proceeding. The cost of capital may thus be computed by calculating the carrier's current cost of debt, current cost of equity and weighing these two figures to reflect the carrier's debt/equity capital structure.

should be excluded from the return on investment. The record here does not permit us to ascertain the amount that the value of the rail property increased. Accordingly, we have declined to make any estimates in our illustration.

In the computation of future subsidy amounts, however, the subsidizer may deduct the annual increase in the value of the property which is due *solely* to inflation from the return on investment which it will be required to pay to the carrier. The burden of showing this increase will fall on the subsidizer.

By applying a 12.1 percent rate of return to an investment base of $1,801,789 (working capital of $10,435; income tax benefits of 0, and net liquidation value of $1,791,354, we computed the total return on investment in our illustration at $218,016.

Maintenance of Way and Structures—Maintenance costs are calculated in accordance with the regulations contained in 49 C.F.R. 1121.43(a). Under these regulations, the carrier is allowed to receive reimbursement for the reasonable expenses incurred to maintain the line at Federal Railroad Administration (FRA) Class 1 safety standards. The railroad may charge for additional expenditures only if the shipper requires a higher level of service.

The Shippers Group believes that the $1,969 per maintrack mile expended by CNW in 1980 should be adequate to maintain the line in reasonable operating condition for the immediate future especially since most of the track is FRA Class 3. CNW estimates the maintenance of way expenditure for the subsidy year will be $103,115 or $5,300 per maintrack mile. According to CNW the line deteriorated from Class 3 to Class 1 due to a policy of keeping its operating losses to a minimum by spending a minimum on

maintenance. CNW contends that costs must increase over last year for the line segment to maintain the minimum FRA Class 1 track safety standards.

The subsidizer must pay *all* maintenance of way costs necessary to maintain the line to meet the minimum FRA standards as well as any additional expenses the subsidizer may authorize. In this case, we believe that CNW adequately supported its claim that $103,115 is needed to maintain the line to meet minimum FRA standards for a Class I line. Thus, we will use this figure for illustrative purposes. Of course, offeror will have to pay the actual maintenance costs whether higher or lower than this estimate.

Casualty Reserve Account

CNW has included in its subsidy calculation $15,000 per year for a casualty reserve account. The Shippers Group did not submit an amount for the casualty reserve account. It states, however, that it does not object to paying CNW for the cost of insurance. It does object to a requirement by CNW that an escrow account of $35,000 be established to cover any losses below the deductible amounts of the supplemental insurance.

Under the regulations, the subsidizer is required to pay the carrier for the cost of insurance for the line segment. It is well established that the subsidizer must bear all risks from operation of the line. However, we do not believe that an escrow account is needed. Any accidents on the line will be covered by insurance, and what is deductible will be paid by the subsidizer. We have already found the offeror to be a financially responsible person with the resources to pay for any accidents occuring on the line during the subsidy period.

Administrative Costs

The Shippers Group asserts that 1 percent of the total revenues attributable to the line during the subsidy period is the proper amount to be assigned as administrative costs. CNW maintains that it can claim during any subsidy year either this 1 percent or the actual cost of administering the subsidy if the cost is higher. CNW derived its administrative costs of $2,481 by taking 1 percent of the total revenues.

We agree with CNW. In *Bloomer Line* we ruled that the carrier may either claim the actual costs of administering the subsidy or claim an amount equal to 1 percent of the revenues attributable to the line. 49 C.F.R. 1121.42(k).

Frequency of Service

CNW's estimated subsidy is predicated upon service being performed either twice or three times per week. The Shippers Group did not specify the frequency of service but expressed the view that the frequency of service should be dictated by the subsidizer, not the railroad. The offeror requests that we clarify this point.

We agree that it is the subsidizer who dictates the frequency of service. However, for purposes of illustration, we will base our subsidy illustration upon service being performed twice a week.

Summary of Illustration

A summary of our calculations for the year ended 1980 is contained in Appendix A. If a subsidy agreement had been in place during the base year, the subsidy required of the Shippers Group would have been $363,769.

We emphasize that the figures used in the appendix are for the purpose of illustration only, not an estimate of actual future expenses. Subsidization figures may vary greatly from the number used in our discussion.

CONCLUSIONS

Pursuant to our power to set conditions in subsidy agreements, we will require the offeror to notify both CNW and the Commission of its decision to accept the terms of this decision or withdraw its offer. This written notification must be submitted to CNW and the Commission within 10 days of the service date of this decision.

This decision will not significantly affect either energy consumption or the quality of the human environment.

It is ordered:

1. The Shippers Group must either withdraw its offer or accept the terms of this subsidy agreement within 10 days of service date of this decision. The notification of acceptance or withdrawal shall be made in writing to the Commission, CNW, and all the parties of record.

2. If the Shippers Group files a timely acceptance of the terms of the subsidy agreement it and CNW shall be bound by the terms and conditions established in this decision.

3. If the Shippers Group does not make a timely written acceptance or withdrawal of its offer, the Commission shall treat the offer as if it were withdrawn.

4. If the Shippers Group withdraws its offer, the Commission shall issue a certificate authorizing the abandonment. The abandonment certificate shall be served within 20 days after the service date of this decision.

5. This decision shall be effective on the date it is served.

By the Commission, Chairman Taylor, Vice Chairman Clapp, Commissioners Gresham and Gilliam.

AGATHA L. MERGENOVICH
Secretary

(SEAL)

Finance Docket No. 1 (Sub-No. 113)

Appendix A

1980 Subsidy Requirement
(Reflects two trips weekly)

Total Revenues	$ 248,051
On-branch Costs	
Maintenance of Way and Structures	$ 103,115
Maintenance of Equipment	8,084
Transportation	111,378
Freight Car Costs	18,542
Return on Investment—	
Locomotives	18,196
Property taxes	—
Total	259,315
Off-branch Costs	117,008
Total Avoidable Costs	376,323
Subsidization Costs For	
Rehabilitation	—
Administrative Costs	2,481
Casualty Reserve Account	15,000
Total Subsidization Costs	$ 17,481
Return on Value for Valuation of Property	
a. Working Capital	10,435
b. Income tax benefit	—
c. Property valuation	1,791,354
Total Investment Base	**1,801,789**
Rate of Return	**12.1%**
Total Return on Value	**$ 218,016**
Estimated Subsidy	**$ 363,769**

APPENDIX E

October 30, 1981

Mrs. Agatha L. Mergenovich, Secretary
Interstate Commerce Commission
12th & Constitution Avenue, N.W.
Washington, D. C. 20423

Re: Docket No. AB-1 (Sub-No. 113F), C&NW Abandonment between Oelwein, Iowa and Randolph, Minnesota

Dear Mrs. Mergenovich:

By decision served October 20, 1981, the Commission established conditions and compensation for financial assistance as to a 19.2-mile segment of the line involved in the above proceeding. That action was taken in response to a request to establish such condition filed by Brownsdale Cooperative Association, et al., referred to in the decision as the "Shippers Group."

The Shippers Group hereby withdraws its offer of financial assistance which gave rise to the decision establishing conditions and compensation for financial assistance.

The Shippers Group intends to seek judicial review of the Commission's decision on the merits failing to deny the abandonment application as to the involved 19.2-mile segment of line.

The Shippers Group continues to strongly disagree with the Commission's interpretation of the abandonment and financial assistance statutes, which interpretation has required the Shippers Group to proceed simultaneously in support of inconsistent position—i.e., opposition to the

merits of abandonment and offering financial assistance as if abandonment had been authorized on a final basis.

Very truly yours,

/s/ THOMAS F. McFARLAND, JR.
Attorney for Brownsdale
Cooperative Association, et al.

TMcF:vh:3000
cc: Ms. Ellen D. Hanson
All parties of record

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